(3)

No. 03-702

In the Supreme Court of the United States

SILVER SAGE PARTNERS, LTD, a California limited partnership; ROBERT E. FILLET, PAUL SABEN, RICHARD L. EARLIX, general partners and individually; MICHAEL S. LINSK; EDWARD MOORE, JR., and ALBERT PIMENTEL,

Petitioners,

v.

CITY OF DESERT HOT SPRINGS,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF IN SUPPORT OF PETITION

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INTRODUCTION AND SUMMARY OF THE ARGUMENT

The City of Desert Hot Springs, California ("City") argues that bankruptcy law is "über alles"; it even, according to the City, supersedes the United States Constitution which makes clear that all power to govern cities belongs to the States of which they are subdivisions, not the bankruptcy courts. Thus, the City argues that Chapter 9 city bankruptcies are plain vanilla bankruptcies and are just like those under all other chapters of the Bankruptcy Act, which means that there should be no review of an order that allows a city bankruptcy to proceed.

While this argument supports the City's avowed purpose in filing for bankruptcy - to evade the State of California's law requiring it to pay all final tort judgments, Congress, in response to this Court's precedent, expressly recognized that the Tenth Amendment to the United States Constitution prevents federal law from preempting the State's right to control its cities or evade state responsibilities. It also specifically provided for an immediate appeal of a bankruptcy court's decision allowing, over objections, a city to enter bankruptcy.

I. The City's speculation that Congress intended no immediate appeal of an order allowing a city into bankruptcy despite the specific reference to that right in the statute (11 U.S.C. 921(e)) and the Circuit conflict on that issue, show that this Court should settle this important question of federal appellate jurisdiction

First, the factual context in which this federal appellate jurisdiction question is presented should be noted. The City

of Desert Hot Springs admits that its bankruptcy is an attempted end run around the dictates of Chapter 9 bankruptcy law which require that it comply with all state laws even those requiring that it pay all final judgments against it. See, e.g., 11 U.S.C. § 943(b)(4) ("The court shall confirm the plan [of adjustment of debts] if [] the debtor *is not prohibited by law*[1] from taking any action necessary to carry out the plan"). Indeed, nowhere in its opposition does the City ever disavow that its purpose in filing bankruptcy is to evade California's requirement that it pay Silver Sage's tort judgment against it[2] (referring dismissively to Silver Sage, which has a final federal question money judgment based upon the Fair Housing Act against it, as just another "unsecured creditor", *see* Opps'n. p. 1).

First, to support the City's claim to the unreviewability of a bankruptcy court's order allowing a city into bankruptcy, it argues that city bankruptcies under Chapter 9 are just like all other bankruptcies. In support, it offers a host of irrelevant case law decided under other provisions of the Bankruptcy Act which are applicable only to business and personal bankruptcies. *See* Opps'n. p. 2, n. 2. However, Chapter 9, which pertains only to local governmental entities, is meant to be rarely available and has strict preconditions to entry which are present in no other type of bankruptcy. The federal courts have all recognized this as true, until the Ninth Circuit spoke in this case. *See, e.g., In re Cottonwood Water & Sanitation Dist.*, 138 B.R. 973, 979 (Bankr. D. CO. 1992) ("Important

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[1] The reference to state law in the Chapter 9 statute is "manifestly to state law". *See United States v. Bekins*, 304 U.S. 27, 49, 58 S. Ct. 811, 82 L. Ed. 1137 (1938).

[2] *See* Appendix pp. 87a-88a (Cal. Gov. Code §§ 970.2 - 970.5).

constitutional issues arise when a municipality enters the bankruptcy arena. Recognizing these problems, Congress consciously sought 'to limit accessibility to the bankruptcy court' by municipalities.").

Secondly, while conceding that Congress spoke directly to the appealability of an order allowing a city into bankruptcy at issue here, the City speculates that Title 11 U.S.C. section 921(e) of chapter 9[3] , which describes what happens *when* (not *if* an appeal is allowed, as the City suggests) an appeal is taken from a bankruptcy court's grant of an "order for relief", only means that the federal courts "may" allow appellate review. The City does not cite a single case or even any legislative history in support of its position. Rather, it seeks to mislead by misstating what the legislative history Silver Sage cites actually says.

In focusing solely upon the Senate version of the 1976 law (as to section 921(e)), the City entirely ignores the fact that the United States House of Representatives' version of the same bill did allow (as did former law) the immediate appeal of a bankruptcy court's grant of an order for relief in a Chapter 9 municipal bankruptcy. More importantly, the transcript of the bankruptcy law reconciliation process

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[3] It was 11 U.S.C. § 405 under the former version of the Chapter for municipal bankruptcies. The text of section 921(e) reads:

> The court may not, on account of an appeal from an order for relief, delay any proceeding under this chapter in the case in which the appeal is being taken; nor shall any court order a stay of such proceeding pending such appeal. The reversal on appeal of a finding of jurisdiction does not affect the validity of any debt incurred that is authorized by the court under section 364(c) or 364(d) of this title.

between the House and Senate versions of the bill emphatically states that the immediate appeal right survived the reconciliation negotiations. *See* Appendix page 109a (*United States Code Congressional and Administrative News*:

> "The proposed text [of the joint and final bill actually enacted] includes compromise language designed to achieve [the reconciliation of the Senate and House versions both allowing *an immediate interlocutory appeal* and the Senate bill's language concerning the no-stay provision during the appeal and validating debt issued by a city in bankruptcy even if the bankruptcy is dismissed as a result of the appeal]."

Finally, the City also claims that there is no conflict between or among the Circuits as to whether an immediate appeal is contemplated by section 923(e) and that all courts have agreed that there is not. Opps'n. pp. 11-12. Its argument on this point is clearly mistaken. The City claims that the *per curiam* Third Circuit opinion in *Pennbank v. Washabaugh* (*In re North and South Shenango Joint Municipal Authority*), 8 BCD 509, 5 CBC2d 869 (3rd Cir. 1981), only decided not to grant a writ because an appeal was available "only after the entry of a final judgment itself". Opps'n. at 11. Not only is that argument supported only by the City's guesswork, but the decision itself and the subsequent history of the case conclusively shows the opposite. *See*, *e.g.*, Appendix p. 116a and 117a, stating that the petition for writ of mandamus challenged the bankruptcy court's order for relief in response to Pennbank's "motion to dismiss" the Chapter 9 bankruptcy for lack of jurisdiction case and noting Pennbank's simultaneous *appeal* of that denial of its motion to dismiss. *See also* the subsequent reported bankruptcy case *In the matter of: North and South Shenango Joint Municipal Authority*, 80 B.R. 57 (WD PA 1982) (the

district court sitting as a reviewing court as to the bankruptcy court's decision to grant an order for relief, dismissed the bankruptcy pursuant to the immediate appeal referenced in the Third Circuit's opinion).

The City is also wrong in stating that the Fifth Circuit agrees with the Ninth that there is no immediate right of appeal of a bankruptcy court grant of an order for relief. In *Path-Science Laboratories, Inc. v. Greene County Hospital* (*In re Greene County Hospital*), 835 F.2d 589, 590 (5th Cir. 1988), the Fifth Circuit (utilizing extensive baseball imagery) never reviewed the grant of an order for relief; rather, it reviewed a bankruptcy court's decision that a debtor was eligible on account of its quasi-governmental status to file a chapter 9, *not* a chapter 11, debtor as it had claimed when it filed. Accordingly, the Third and Ninth Circuit decisions conflict on the immediate appeal question.

II. An order allowing a city into bankruptcy is sufficiently final - because it is unreviewable later; and is the "final" word on Congress's preconditions for a city to enter bankruptcy; and because of the significant prejudice to creditors, taxpayers and the public - to qualify as immediately appealable under this Court's "collateral order" doctrine

The City seeks to mislead this Court on the "collateral order" discussion as well. It first claims that the Ninth Circuit stated that the question of whether the bankruptcy should be allowed in the first place is reviewable later - after the bankruptcy has been completed. *See* Opps'n. p. 8. Its sole support for this is a quote from the Ninth Circuit's opinion that, in fact, says no such thing. The quote references not the issue of reviewability of the Bankruptcy Court's decision as to the propriety of the bankruptcy filing,

but instead notes that the bankruptcy judge's ongoing power to supervise the bankruptcy proceedings allows it to dismiss a Chapter 9 bankruptcy case if the bankruptcy court becomes convinced that the city is acting in bad faith *in the conduct of the bankruptcy*.[4] *Silver Sage Partners, Ltd. v. City of Desert Hot Springs* (*In re City of Desert Hot Springs*), 327 F.3d 930, 936 (9th Cir. 2003) (". . . . *If it does appear, at some [later] time*, that the City is failing to act in good faith[in the bankruptcy proceeding], the bankruptcy court may dismiss the petition altogether.").

More importantly in terms of this Court's "collateral order" doctrine analysis[5], the City never shows that the three prongs of that test are not met (a conclusive determination as to the qualification of a city to be in bankruptcy; that the question of a city's qualification to file bankruptcy is separate

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[4] Moreover, the City's argument conflates the analysis of a bad faith filing with the bad faith conduct of a case and the proposing of a bankruptcy "plan" in bad faith. These are three separate, albeit related, matters and, most assuredly, are not treated as one and the same by the courts. *See In re Sullivan County Regional Refuse Disposal Dist.*, 165 B.R. 60, 80 (D NH 1994) ("Chapter 9 is the only chapter which currently expressly mentions good faith"); *In re Miracle Church of God in Christ*, 119 B.R. 308 (MD FL 1990) ("this standard of good faith is implicit in every stage of a bankruptcy case").

[5] A collateral order is reviewable under *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 546 (1949), if it (i) conclusively determines the question present; (ii) resolves an important issue that is completely collateral to the merits; and (iii) concerns a right that would be effectively unreviewable after a final judgment on the merits. *See Gulfstream v. Mayacamas Corp.*, 485 U.S. 271, 276, 108 S. Ct. 1133, 99 L. Ed. 2d 296 (1988).

from the merits of who gets paid what in the bankruptcy itself and that that determination is unreviewable later).

Indeed, all three prongs are present here. Since a city's qualification to enter bankruptcy is conclusively determined at the outset, the meeting of the relevant Congressional factors are clearly not reviewable later after the bankruptcy has already been completed; that question is only reached once - at the beginning of the bankruptcy. The City also does not and cannot explain why the question of qualification to be in bankruptcy is not separate from the merits of who gets paid what in the bankruptcy. Indeed it is clear, that whether a city meets Congress's disclosure and negotiation requirement before filing, filed for a proper purpose, or is actually insolvent under Congress's definition, are separate from the merits of a confirmed bankruptcy plan. Thus, such questions as whether a city improperly gerrymandered claims to employ "cram down" upon a specific creditor or whether its plan complies with all state laws, are clearly separate from whether a city is actually insolvent as Congress defines it, whether it negotiated a confirmable plan before filing, etc.[6]

Finally, the City argues that if there is no immediate appeal, there is no prejudice to any party. *See* Opps'n. p. 9. In fact, for several reasons unaddressed by the City, this is not true. First, Congress eliminated prejudice to the debtor *City* by its provision of an immediate appeal right to creditors or other interested parties. *See* 11 U.S.C. § 921(e), which prevents a city's bankruptcy from being stayed during the appeal and provides that any debt undertaken by a city in bankruptcy while the appeal is pending is valid even if the bankruptcy is dismissed incident to the appeal.

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[6] All showings required by 11 U.S.C. § 109(c).

The City also never mentions that the prejudice to the creditors of a city, its employees and its taxpayers, is palpable if there is no immediate appeal. Because Congress's preconditions are decided only once and the bankruptcy court may be in error as to one or more of them, Congress's important preconditions such as proof of insolvency, etc., are rendered advisory only if there is no immediate appeal.

Additionally, since a bankruptcy court cannot, for Tenth Amendment reasons, control a city in bankruptcy or appoint a trustee, limit its spending or operations or prevent dissipation of its assets, a city is free to, as has already occurred here, not pay a penny to its creditors or its employees during the bankruptcy (as to pre-petition wages or pension contributions) or even ignore obligations to pay tax refunds to its taxpayers. All the while, it may spend however it wishes and encumber or sell any of its property at its unbridled discretion. This is why Congress made entry into Chapter 9 difficult, which, in and of itself, supports the view that an immediate appeal of bankruptcy orders allowing a city into bankruptcy are appealable. *See* Congress' requirements of 11 U.S.C. § 109(c); and *In re Cottonwood Water & Sanitation Dist.*, 138 B.R. at 979.

CONCLUSION

This Court should review and settle the important federal jurisdictional question of whether there is an immediate appeal of the "jurisdictional" determination by a bankruptcy court to allow a city to enter bankruptcy. Since this decision necessarily carries with it complicated Federal and State power issues and extensive prejudice to the city's residents, its creditors, employees and the business community, Congress made such decisions reviewable as of right. They

should also be reviewable under the Court's "collateral order" doctrine in any event.

Dated: December 23, 2003

Respectfully Submitted,

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